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Sec. 101 3

Sec. 102 2

In the Supreme Court of the United States

OCTOBER TERM, 1962

No.

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ISABELLE M. KUNTZ, INDIVIDUALLY AND AS EXECUTRIX OF THE ESTATE OF MARTIN KUNTZ, SR., DECEASED

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

The Solicitor General, on behalf of the Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the decision of the United States Court of Appeals for the Sixth Circuit in the above-entitled case.

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 43a-47a [1]) is not officially reported. The opinion of the court of appeals (App. 11-18) is reported at 300 F. 2d 849.

[1] "R." refers to the appendix to the taxpayer's brief in the court of appeals; "App." to the appendix to this petition.

JURISDICTION

The judgment of the court of appeals was entered on April 4, 1962 (App. 18). On July 3, 1962, by order of Mr. Justice Stewart, the time within which to file a petition for a writ of certiorari was extended to and including September 1, 1962. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Upon the death of an officer of a corporation, the board of directors authorized the payment, out of corporate assets, of $42,000 to his widow. The question is whether the payment so authorized was excludible from the widow's gross income as a "gift" under § 102(a) of the Internal Revenue Code of 1954.

STATUTE INVOLVED

Internal Revenue Code of 1954 (26 U.S.C.):

> Sec 102. Gifts and Inheritances.
>
> (a) General Rule.—Gross income does not include the value of property acquired by gift, bequest, devise, or inheritance.
>
> * * * * *

STATEMENT

Martin C. Kuntz, Sr., died on January 3, 1955. He was then the president, and had for 42 years been an officer, of The Peter Kuntz Company, a family-owned corporation in which he held a minority stock interest (approximately 10,000 shares). At the date of his death, his salary ($42,000 a year) had been fully paid, and there was no contract, practice, or understanding

requiring the corporation to make any further payments (R. 22a, 29a, 38a, 44a).

On January 7, 1955, the board of directors of the Company resolved (R. 14a):

> * * * that because of Martin C. Kuntz, Sr.'s service of forty-two (42) years * * * and because during this entire period until his death he devoted all of his time, skill and knowledge to the welfare of this corporation; it is to the best interests, and benefit of the corporation to pay to Isabel M. Kuntz, the widow of Martin C. Kuntz, Sr. deceased, the sum of $42,000.00 which was the amount of his yearly salary for 1954, payable in twenty-four semi-monthly installments beginning January 15, 1955. This payment is made as additional compensation and in consideration of services heretofore rendered to this corporation by the late Martin C. Kuntz, Sr. as hereinbefore stated.

Pursuant to that resolution, the corporation paid Mrs. Kuntz $42,000 during the calendar year 1955.[2] The corporation withheld income taxes from the payments and deducted them on its return as "employee salary expense" (R. 45a). Mrs. Kuntz, however, treated the payments as "gifts" excludible from income under § 102(a) of the Internal Revenue Code of 1954 and did not report them as income. The Commissioner held

[2] An additional $5,000 was paid under a second resolution, adopted at the same time, which described the payment as an "employee benefit" paid "in accordance with" § 101(b) of the Code (R. 14a). That payment was admittedly excludible from income as an employee death benefit under § 101(b) and is accordingly not in issue.

that the payments were not gifts and determined a deficiency accordingly. In due course, the taxpayers (Mrs. Kuntz and her husband's estate, with which she had filed a joint return) petitioned the Tax Court for a redetermination of the deficiency.

Apart from the above facts, the only material evidence offered at the trial was the following testimony of William Kuntz and Edward Kuntz who, as officers and directors of the corporation, had voted for the resolution:

[*William Kuntz—Direct* (R. 22a)]

Q. From the discussions at the board meeting, will you please state the purpose and intention of the resolution to pay $42,000 to Isabel Kuntz?

A. In the discussion at the directors' meeting of the intent, and certainly my intent, and I am sure of the balance of the directors, that this was a gift to Mrs. Kuntz.

* * * * *

[*Cross-Examination* (R. 23a)]

A. Why that exact wording [of the resolution] was used, I do not recall. It is one of those things that you write up your resolution, and sort of think that you have it in writing the way you are thinking that it should be.

Q. And so this resolution was the way—as it was written, the way at that time you intended it to be written?

A. Well, as I stated before, we intended it as a gift.

Q. Did you intend this resolution to state as you voted for it; the language it contains?

A. We thought it was a gift, because of the fact that Mrs. Martin Kuntz, Sr., had never worked for or performed any services for the corporation.

Q. You are not answering my question, sir. Did you intend—Were you voting—Did the language of this resolution, did it reflect your intentions when you voted for it, sir?

A. Yes, the language in the resolution means that it is a gift, that's what we were voting for, a gift.

Q. So the language says that the payment is made as additional compensation, and in consideration of services heretofore rendered to this corporation by the late Martin C. Kuntz, Sr., as hereinbefore stated, that was erroneous you mean?

A. If compensation means receiving money for work done, it is erroneous.

* * * * *

[*Edward Kuntz—Direct* (R. 29a)]

Q. Can you state from your knowledge and recollection of what transpired at that board meeting what the purpose and intention of the $42,000 resolution was?

A. It was intended to be a gift.

* * * * *

[*Cross-examination* (R. 30a)]

Q. Mr. Kuntz, could you explain to the court why this language in the resolution authorizing the $42,000 payment to Mrs. Kuntz contains the specific language, "This payment is made as additional compensation and in consideration of services heretofore rendered to this corporation by the late Martin C. Kuntz, Sr., as hereinbefore stated"?

A. It was just a matter of expressing the gift that was given to Mrs. Martin Kuntz.

* * * * *

The Tax Court, in a memorandum decision, found as a fact that the $42,000 was paid to Mrs. Kuntz "for the reasons and purposes set forth in the resolution" and held that a payment made for those reasons was not a gift (R. 43a-47a). The Court of Appeals for the Sixth Circuit reversed, holding that "the only reasonable inference" to be drawn from the evidence was that "the intent of the transferor was to make a gift"—an inference compelled by the testimony of the two directors that a "gift" was "intended," the fact that Mrs. Kuntz had performed no services, and the absence of any obligation to pay more for those of Mr. Kuntz (App. 16-18).

REASONS FOR GRANTING THE WRIT

1. The decision below is in conflict with the decisions of the Third Circuit in *Smith* v. *Commissioner* and *Martin* v. *Commissioner*, decided on June 28, 1962.[3] The *Smith* and *Martin* opinions are printed in the appendix at pp. , *infra*.

[3] Petitions for rehearing in *Smith* and *Martin* were denied on August 15, 1962.

The conflict arises from the Tax Court's recent reappraisal and reversal of its position on the taxability of widow bonuses. Begining with *Aprill* v. *Commissioner*, 13 T.C. 707, and until this Court's decision in *Commissioner* v. *Duberstein*, 363 U.S. 278, the Tax Court consistently held widow bonuses to be gifts excludible from income.[4] Following the clarification of the meaning of the gift exclusion in *Duberstein*, however, the full Tax Court reconsidered the question and, in *Pierpont's Estate* v. *Commissioner*, 35 T.C. 65, in effect overruled its prior decisions. With the same consistency that it had previously held widow bonuses to be gifts, the Tax Court now holds them to be income.[5]

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[4] E.g., *Macfarlane* v. *Commissioner*, 19 T.C. 9; *Hellstrom's Estate* v. *Commissioner*, 24 T.C. 916; *Maycann's Estate* v. *Commissioner*, 29 T.C. 81; *Luntz* v. *Commissioner*, 29 T.C. 647; *Hahn* v. *Commissioner*, decided March 31, 1954 (1954 P-H T.C. Mem. Dec. ¶ 54,103); *Reardon's Estate* v. *Commissioner*, decided June 15, 1955 (1955 P-H T.C. Mem. Dec. ¶ 55,154); *Haskell* v. *Commissioner*, decided July 19, 1955 (1955 P-H T.C. Mem. Dec. ¶ 55,196); *Matthews* v. *Commissioner*, decided February 29, 1956 (1956 P-H T.C. Mem. Dec. ¶ 56,046; *Mann* v. *Commissioner*, decided March 28, 1957 (1957 P-H T.C. Mem. Dec. ¶ 57,049); *Hekman's Estate* v. *Commissioner*, decided April 30, 1957 (1957 P-H T.C. Mem. Dec. ¶ 57,070); *Morse's Estate* v. *Commissioner*, decided March 31, 1958 (1958 P-H T.C. Mem. Dec. ¶ 58,051).

[5] In addition to *Pierpont* and this case, see *Martin* v. *Commissioner*, 36 T.C. 556, affirmed June 28, 1962 (C.A. 3); *Westphal* v. *Commissioner*, 37 T.C. 340, pending on appeal (C.A. 8, No. 17059); *Penick* v. *Commissioner*, 37 T.C. 999, pending on appeal (C.A. 3, No. 14089); *Russek's Estate* v. *Commissioner*, decided January 31, 1961 (1961 P-H T.C. Mem. Dec. ¶ 61,028); *Fischer* v. *Commissioner*, decided February 28, 1961 (1961 P-H T.C. Mem. Dec. ¶ 61,061); *Cooper's Estate* v. *Commissioner*, decided May 29, 1961 (1961 P-H T.C. Mem. Dec. ¶ 61,154); *Smith* v. *Commissioner*, decided May 29, 1961 (1961 P-H T.C. Mem. Dec. ¶ 61,155), affirmed June 28, 1962 (C.A. 3); *Olsen's Estate* v. *Commissioner*, decided May 31, 1961 (1961 P-H T.C. Mem. Dec. ¶ 61,161), reversed, 302 F.2d 671 (C.A. 8); *Cronheim's Estate* v. *Commissioner*, decided August 17, 1961 (1961 P-H T.C. Mem. Dec. ¶ 61,232), pending on appeal (C.A. 8).

Appeals by taxpayers challenging the Tax Court's change of heart have produced, during a four-month span (March-June 1962), no fewer than five opinions by four courts of appeals. The first, that of the Fourth Circuit in [*Pierpont's Estate*] v. *Commissioner*, 301 F. 2d 287, was inconclusive, with the case being remanded to afford the parties an opportunity to offer additional evidence in the light of the new standards being applied. The second was the decision of the Sixth Circuit in this case (*Kuntz*), which reversed the Tax Court outright and held the payment to be a gift. The Sixth Circuit was followed, with the same result, by the Eighth Circuit in *Olsen's Estate* v. *Commissioner*, 302 F. 2d 671, in which we are simultaneously filing a petition for certiorari. Finally, the Third Circuit took a contrary view and, in *Smith* v. *Commissioner*, and *Martin* v. *Commissioner* (pp. 19-33, *infra*), affirmed, as not clearly erroneous, Tax Court decisions holding widow bonuses to be taxable as income.[6]

The conflict between the *Kuntz* and *Olsen* cases, on the one hand, and the *Smith* and *Martin* cases, on the other, is evident from the opinions, for there are no differences of fact that could explain different results even in the trial courts, much less on appellate review of substantially identical findings.[7] The conflict was

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[6] Appeals are pending in three other Tax Court widow-bonus cases, *Westphal* v. *Commissioner*, *supra* (C.A. 8, No. 17059); *Cronheim's Estate* v. *Commissioner*, *supra* (C.A. 8, No.); and *Penick* v. *Commissioner*, *supra* (C.A. 3, No. 14089). Since the appeals are pending in the same courts that decided *Olsen* (C.A. 8) and *Smith* and *Martin* (C.A. 3), however, they have been held in abeyance by counsel pending the final disposition of those cases.

[7] The testimony of the two directors that "we intended it as a gift" (see Statement) affords no basis for distinction, for the testi-

acknowledged by the Third Circuit, which, in affirming the Tax Court, took note of the reversals of similar Tax Court decisions in this case and in *Olsen* but observed that "We cannot exceed the narrow function assigned to us, regardless of what others have done." (pp. 27-28, *infra*). We need not now consider whether the conflict is attributable, as the Third Circuit suggests, to a difference in the scope of review or, rather, to an underlying difference in the courts' conception of what constitutes a gift, for in any event there is an irreconcilable difference of result: the Third Circuit would have affirmed the Tax Court decisions in this case and in *Olsen* and the Sixth and Eighth Circuits would have reversed in *Smith* and *Martin*. To resolve that conflict, certiorari should be granted.

2. The question is important. Voluntary payments to widows of corporate officers (typically, as here, of a year's salary) are commonplace, and their tax treatment has posed an administrative and judicial problem of significant proportions. There are now pending in the district courts about 50 such cases, and the Commis-

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mony was devoid of content other than as an ultimate legal characterization of the transaction, which it is the court's and not the witness' function to make. The meaninglessness of such testimony is, indeed, sharply demonstrated by the record here, for one of the directors, having so testified, made the mistake of explaining, in response to the next question, what he meant (R. 23a):

> We thought it was a gift, because of the fact that Mrs. Martin Kuntz, Sr. had never worked for or performed any services for the corporation.

What his testimony that he "intended" the payment "as" a gift meant, in short, was that Mrs. Kuntz had performed no services, a conceded fact true of all the cases. That, under the witness' definition of the term, that circumstance made the payment a "gift" is of course, an irrelevancy.

sioner is holding over 450 more in suspense awaiting the outcome of the present litigation. The revenue involved is substantial (the 500 pending cases involve approximately $5,000,000 in taxes), but even more pressing is the need to have the question resolved in order that the existing backlog of cases—and the new cases arising almost daily—can be disposed of without flooding the courts with litigation.

CONCLUSION

For the reasons stated, the petition for certiorari in this case should be granted. See also the petitions being simultaneously filed in two other widow-bonus cases, *Commissioner* v. *Olsen* and *United States* v. *Frankel*.

Respectfully submitted,

ARCHIBALD COX,
Solicitor General.

LOUIS F. OBERDORFER,
Assistant Attorney General.

WAYNE G. BARNETT,
Assistant to the Solicitor General.

AUGUST 1962.

APPENDIX

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

ESTATE OF MARTIN KUNTZ, SR., DECEASED, ISABELLE M. KUNTZ, EXECUTRIX, AND ISABELLE M. KUNTZ, INDIVIDUALLY, SURVIVING WIFE, PETITIONERS,

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

Decided April 4, 1962

Before: O'SULLIVAN, Circuit Judge, and DARR and THORNTON, District Judges.

THORNTON, District Judge. The only question on this review of the decision of the Tax Court is whether the one *determinative* finding of fact by the Tax Court is "clearly erroneous." All the findings of fact contained in the Memorandum Decision of the Tax Court are findings of fact based on undisputed or conceded facts. None, save the determinative one above adverted to, constitutes the resolution of any factual issue. In ascertaining what standard is to be applied for the purpose of "clearly erroneous" we are not without definitive guidance. Section 7482 of the Internal Revenue Code of 1954 provides that "The United States Courts of Appeals shall have exclusive jurisdiction to review the decisions of the Tax Court, . . ., in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury." Rule 52(a) F. R. Civ. P. provides that the findings of fact by a district court in a non-jury case "shall not be

set aside unless clearly erroneous." In *Commissioner* v. *Duberstein*, 363 U. S. 278, 291 (1960) the Supreme Court has explicitly negatived the possibility that the findings of the Tax Court are of any different weight. In *Duberstein*, at page 291, the Court reiterates what it said 12 years earlier in *United States* v. *United States Gypsum Co.*, 333 U. S. 364, 395—" 'A finding is "clearly erroneous" when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed.' " *Duberstein*, at page 291, reiterates, also from *Gypsum*, that the "rule itself applies to factual inferences from undisputed facts, id, at 394, as will on many occasions be presented in this area."

The only issue presented to the Tax Court for determination was whether the payment to Mrs. Kuntz of $42,000 by her deceased husband's employer was taxable income. The Commissioner of Internal Revenue determined that it was, and assessed an income tax deficiency in the amount of $13,189.11 for the year in question—1955. The position of petitioners is that the payment constituted a gift within the meaning of section 102 of the Internal Revenue Code of 1954 and therefore does not constitute taxable income.

The factual background here is simple. Martin Kuntz died January 3, 1955 having devoted his entire working life of 42 years to the Peter Kuntz Company. His salary had been $42,000 annually from 1951. He had been president of the company from 1954. On January 7, 1955 (four days after his death) the board of directors at a special meeting passed the following resolution:

> "WHEREAS, Martin C. Kuntz, Sr., our beloved brother, who died January 3, 1955, had completed

42 years of faithful service to The Peter Kuntz Company, and

"WHEREAS, Martin C. Kuntz, Sr. as President of this company from August 5, 1954 until his death, and prior thereto as executive Vice-President and Secretary, did direct the affairs of the company in a highly successful manner,

"BE IT RESOLVED, That the Directors of the company hereby record their deep appreciation for the many contributions of Martin C. Kuntz, Sr., his loyalty, boundless energy, untiring efforts, excellent judgment and splendid leadership.

"It was moved by Elizabeth K. Wickham, seconded by John J. Kuntz, and upon vote unanimously passed, that because of Martin C. Kuntz, Sr.'s service of Forty-Two (42) Years to The Peter Kuntz Co., in an executive capacity, as outlined in the above Resolution, and because during this entire period until his death he devoted all of his time, skill and knowledge to the welfare of this corporation; it is to the best interests, and benefit of the corporation to pay to Isabelle M. Kuntz, the widow of Martin C. Kuntz, Sr., Deceased, the sum of $42,000.00 which was the amount of his yearly salary for 1954, payable in twenty-four semi-monthly installments beginning January 15, 1955. This payment is made as additional compensation and in consideration of services heretofore rendered to this corporation by the late Martin C. Kuntz, Sr. as hereinbefore stated."

A second resolution for the payment of $5,000 to the widow was also passed at this time, but since it is not relevant to this discussion it will not be referred to again.

It is perfectly clear that the $42,000 resolution states that payment is made "as additional compensation and in consideration of services heretofore rendered to this corporation by the late Martin C. Kuntz, Sr." The question is: Does this characterization *control* as to the true nature of the payment? Testimony was taken before the Tax Court from four witnesses. Two were directors of the corporation. They stated unequivocally that the intention had been to make a gift. A third witness was the controller of the company. His testimony was barren of any information that was illuminating as to gift versus compensation. The widow also testified. Her testimony indicated that she was unaware of the resolution until after it was passed. She gave no illuminating testimony as to the gift versus compensation aspect other than to say she was not and never had been employed by the company had never performed any services for it, and at the time of her husband's death she owned no stock in the company.

On these facts the Tax Court found in the only determinative paragraph of its findings that the $42,000 was paid "for the reason and purposes set forth in the resolution of the board of directors of the corporation authorizing such payment, and was not a gift within the meaning of section 102 of the Code of 1954." The Tax Court in its Memorandum Decision does not expressly state that the language of the resolution controls its decision. However, there is nothing present in the record other than this language to provide the basis for such a determination. The Tax Court refers to the *Reed* case (*Reed* v. *United States*, 177 F. Supp. 205, aff'd 277 F. 2d 456, 6 Cir., 1960) as being factually different. The only relevant factual difference is to be found in the presence in *Reed* of a statement of the purpose of the payment as being "a material expression

of sympathy, generosity and kindness to the widow of a deceased officer and employee," which is not present in the instant case, and the presence in the instant case of a statement of purpose as being compensatory, which is not present in *Reed*. It is this difference upon which the Tax Court relied in distinguishing between *Reed* and the instant case. In all other pertinent respects the facts are practically identical. In *Reed*, this Court affirmed the determination of the Tax Court that the payment was a gift and not taxable income. The Tenth Circuit Court of Appeals, on November 1, 1960, just three weeks prior to the Memorandum Decision of the Tax Court in the instant case, rendered an opinion affirming on facts almost identical to those in the instant case the determination of the trial court that the payment to the widow was a gift. The resolution there stated the purpose as being "in recognition of the services rendered by her husband, A. W. Ainsworth, to this corporation." *United States* v. *Kasynski*, 284 F. 2d 143, 144, 10 Cir., 1960.

The case before us for review presents no basic factual dispute. The dispute arises from the factual inferences to be drawn from the particular language employed characterizing the nature of the payment. The fact that a transaction is stated to be a particular type of transaction does necessarily mean that it is that type. In *Duberstein*, supra, the parties to the transfer both stated it to be a gift. The Supreme Court held otherwise. The classic instance, of course, is where the transfer of title to real estate has been held by the courts again and again to be a mortgage and not a conveyance of ownership to the land despite the strongest kind of language employed in the deed of transfer. There are probably few courts in the land which have not been called upon to determine whether an instru-

ment entitled "conditional sale" is not actually a chattel mortgage. There is no reluctance on the part of the courts to declare a transaction to be what it essentially is regardless of how the parties have denominated it.

We hereby adopt the reasoning and rationale of the *Kasynski* case (284 F. 2d 143, 10 Cir., 1960) in relation to the merits of the instant case. In that opinion the court found that the finding of the lower court—that the intent of the transferor was to make a gift—was a reasonable inference from the "factual pattern" there present. We here hold that such a finding is the only reasonable inference from the "factual pattern" *here* present, and that the contrary factual finding by the Tax Court leaves us with "the definite and firm conviction that a mistake has been committed." In addition to the uncontradicted and unimpeached testimony of the two directors that a gift was intended there exist certain realistic aspects. Clearly, the widow herself was not being compensated. Clearly, the corporation anticipated no economic benefit as a result of the payment. Quite different is the situation in *Duberstein* (363 U. S. 278, 1960) where the taxpayer himself rendered services for which he was not compensated, and where the transferor was not only obligated in a moral and economic sense but where he might well be anticipating receiving further such services. We have none of that here. Nor is there a shade of indication that the deceased officer and employee was not fully compensated for all services rendered by him to the transferor corporation. His salary was $42,000 a year and had been that for four years immediately preceding his death. In *Duberstein* (363 U. S. 278, 292) the Supreme Court said that the conclusion of the Tax Court "appears based in the sort of informed experience with human affairs that fact-finding tribunals

should bring to this task." While we are admonished not to substitute our judgment for that of the trial court, we are convinced and persuaded that "informed experience with human affairs" not only dictates but compels the conclusion that the Tax Court erred and committed a mistake in its finding and conclusion that compensation was the dominant reason for the transfer rather than sympathy, generosity and kindness to the widow of an officer and an employee of 42 years, who had devoted all of his working life to the success and prosperity of the company. As we have previously set forth, the *only* indicia of compensatory motivation is the one statement in the resolution. Concerning the inclusion of this self-serving statement, the witness William Kuntz, one of the two directors who testified at the Tax Court proceeding, was asked on cross-examination why the language in the resolution stated that the payment was made as additional compensation. His answer was as follows: "Why that exact wording was used, I do not recall. It is one of those things that you write up your resolution, and sort of think that you have it in writing the way you are thinking that it should be." Edward Kuntz, the other director who testified, was asked a similar question on cross-examination. His answer was that "[I]t was just a matter of expressing the gift that was given to Mrs. Martin Kuntz." Both of these answers negative the intention of compensation as do the facts that (1) the deceased was fully compensated during his lifetime for the services rendered by him to the corporation; (2) his widow never performed any services for the corporation, nor was there any agreement or plan that she ever would; and (3) that within four days of the death of Mr. Martin Kuntz the directors met for the purpose of passing the resolution that would provide Mrs. Mar-

tin Kuntz with the assurance of economic security for the immediate future. This latter surely spells out motivation by kindness and sympathy rather than by considerations of compensation."

Since the Court "on the entire evidence is left with the definite and firm conviction that a mistake has been committed," the decision of the Tax Court is reversed.

JUDGMENT

April 4, 1962

On Petition to Review a decision of the Tax Court of the United States.

This cause came on to be heard on the transcript of record from the Tax Court of the United States and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this court that the decision of the said Tax Court in this cause be and the same is hereby reversed.

Approved for entry:

/s/ THOMAS P. THORNTON,
United States District Judge.

UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 13,815

MILDRED W. SMITH, PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

Argued March 5, 1962

Before STALEY, HASTIE and SMITH, *Circuit Judges*

[OPINION OF THE COURT]

(Filed June 28, 1962)

By STALEY, *Circuit Judge.*

The question on this appeal is whether the Tax Court's finding that certain payments made by a corporation to the widow of a deceased officer did not constitute a gift is clearly erroneous.

Mildred W. Smith, petitioner on this appeal, is the remarried widow of Norman F. Wiss, who died on September 15, 1954. Prior to his death, deceased had been an employee of J. Wiss & Sons Co. ("corporation") for thirty-five years. Pursuant to a resolution passed by its board of directors, the corporation paid petitioner $38,841.37 in 1955 and $33,008.04 in 1956.[1] Petitioner failed to report these payments as income.

[1] In the year 1954, the corporation also paid petitioner a $5,000 death benefit and $16,000 in periodic payments. These payments are not in dispute here.

The Commissioner concluded that the payments constituted ordinary income and assessed a deficiency against petitioner which the Tax Court upheld.[2] The Tax Court found as a fact that the "dominant motive behind these payments was to give tangible recognition (by way of additional compensation) to the highly valuable services rendered by the decedent over a long period of time," and that the payments were not made as a gift to petitioner.

On appeal, petitioner contends that the Tax Court erroneously concluded that the Supreme Court in Commissioner v. Duberstein, 363 U.S. 278 (1960), changed the law regarding the criteria relevant in resolving the factual inquiry as to whether the payments constituted a gift, and that when the facts of this case are considered in light of the criteria before *Duberstein*, the payments clearly were gifts.[3] The Commissioner, on the other hand, contends that under *Duberstein* the question is purely factual, and the Tax Court's findings here must be affirmed unless they are clearly erroneous.

Because of the importance that the parties attach to Commissioner v. Duberstein, supra, we think it advisable to review in some detail the facts and holding of that decision. *Duberstein* involved two separate

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[2] The Tax Court's findings and opinion are not officially reported.

[3] In this regard, petitioner lists the following factors which she contends were decisive in past Tax Court decisions: (1) payments were made to the widow rather than to the husband's estate; (2) transferee never performed any service for the corporation; (3) the corporation was under no obligation to deceased or transferee to make the payments; (4) deceased was fully and adequately compensated for all services he performed to the corporation; (5) the corporation derived no benefits from the payments; (6) the corporation did not characterize or treat the payments as compensation.

appeals.[4] In one, the taxpayer had received an automobile from a business associate which he failed to report as income, deeming it to be a gift. The other appeal involved payments made by an employer to an employee who had resigned his position. The Supreme Court concluded that the Tax Court's finding that the transfer of the automobile did not constitute a gift was not clearly erroneous, and remanded the other appeal to the trial court for more explicit findings of fact as to whether the payments constituted a gift. The Court refused the Commissioner's invitation to spell out a new test for resolving the question of gift versus income. What ultimately controls, it said, is the intention of the transferor. In making this determination, the proper criteria are those that logically disclose the reason for the transferor's action—"the dominant reason that explains his action in making the transfer." 363 U.S. at page 286. The mere absence of a moral or legal obligation to make the payments does not establish a gift, and a voluntary transfer of property without any consideration or compensation, therefore, although it constitutes a common law gift, is not necessarily a gift within the tax statutes. Reviewing prior decisions, the Court, at 363 U.S. 285, said: "A gift in the statutory sense, on the other hand, proceeds primarily from a 'detached and disinterested generosity' * * * out of affection, respect, admiration, charity or like impulses." If the payment proceeds, however, primarily from a moral duty or legal obligation, or finds its genesis in an anticipated benefit that is economic in nature, it is not a gift. But the presence or absence of economic benefit is irrelevant

[4] No. 376, Commissioner v. Dubenstein; No. 546, Stanton v. United States.

where the transfer is made in return for services rendered.

The Commissioner contended in *Duberstein* that payments made by an employer to an employee are by and large taxable as income, and that the concept of a gift is inconsistent with the payments being deductible as business expenses, and that since a gift involves personal elements, a business corporation cannot make a gift of its assets. The Court refused to adopt these so-called "principles" or "presumptions," saying:

> "Decision of the issue presented in these cases must be based ultimately on the application of the fact-finding tribunal's experience with the mainsprings of human conduct to the totality of the facts of each case. The nontechnical nature of the statutory standard, the close relationship of it to the data of practical human experience, and the multiplicity of relevant factal elements, with their various combinations, creating the necessity of ascribing the proper force to each, confirm us in our conclusion that the primary weight in this area must be given to the conclusions of the trier of facts." 363 U.S. at 289.

United States v. Kaiser, 363 U.S. 299 (1960), was decided the same day as *Duberstein*. In *Kaiser*, the jury determined that strike benefits by way of room rent and food vouchers, rendered by a labor union to striking members, constituted a gift. The trial judge, however, entered judgment n.o.v. in favor of the government, concluding that the assistance constituted income as a matter of law. In concluding that the jury's finding should not have been put aside, the Court reviewed the facts and unmistakably delineated the scope of appellate review:

"* * * the jury could have concluded that assistance, rendered as it was to a class of persons in the community in economic need, proceeded primarily from generosity or charity, rather than from the incentive of anticipated economic benefit. We can hardly say that, as a matter of law, the fact that these transfers were made to one having a sympathetic interest with the giver prevents them from being a gift. * * *

"We need not stop to speculate as to what conclusion we would have drawn had we sat in the jury box rather than those who did. *The question is one of the allocation of power to decide the question; and once we say that such conclusions could with reason be reached on the evidence, * * * our reviewing authority is exhausted* * * *.*" (Emphasis supplied.) 363 U.S. at 304-305.

In summary, determination of whether a transfer constitutes a gift is a factual one, which must be made on a case-by-case approach, resting with the trier of fact which is to make it in light of all the relevant facts and circumstances. Thus, under *Duberstein* and *Kaiser,* such a determination must be affirmed unless it is clearly erroneous.

A review of the record convinces us that the Tax Court did not rely on irrelevant facts and circumstances, that its finding is a permissible one and is not clearly erroneous. In 1948 and again in 1953, the board of directors considered the adoption of a pension plan for its employees that was to be supplemented by payments to the officers' widows. One of the reasons given for not adopting the program of supplemental payments was that the board thought it inappropriate to make arrangements for officers that the corporation

could not afford for other employees. Between 1951 and decedent's death, the corporation made death payments to the widows of four employees. The payments, as here, were made monthly for varying periods, although in amounts substantially less than petitioner received. The four deceased employees were, however, salesmen, not executives, but received salaries in excess of $10,000. The deceased, on the other hand, received an annual salary of $80,000 at the time of death and had been associated with the corporation as officer, director or employee for over thirty-five years. Although the widows were not precluded from disclosing the payments, the corporation sought to receive no publicity for them.

When Norman F. Wiss died, the corporation had fifty-seven common stockholders. Decedent and petitioner held approximately 7.7% of the stock, while most of the remaining major stockholders were related to decedent. Large blocks of stock were held by the estate of decedent's father, and by his sister, brother, nephew and cousin. Four board members attended the September 23, 1954, meeting that authorized the payments in question. One was decedent's brother, two were his cousins, while the fourth was a nephew.

The first resolution adopted by the board that day read as follows:

> "Resolved, that the following memorial be inscribed in the minutes of the directors of the company, and that a copy thereof be sent to Mildred S. Wiss, the surviving widow of Mr. Norman F. Wiss:
>
> "The passing of a relative and associate and friend is always difficult to accept; and it is

particularly so in the case of Norman F. Wiss with whom we were in close association for many years.

"Norman had been a director of the company for 35 years, and for 23 years he was vice president and treasurer, all of which offices he filled with distinction and with great benefit to the company.

"The sound financial condition of the company and its excellent reputation throughout the world are attributable in a large measure to the tireless energies, sound business judgment, high ideals and farsightedness of Norman. We owe a great deal to him, and we take this opportunity of expressing our gratitude for his valuable and loyal services and our deepest regret over his sudden and early death."

The second provides that

"Whereas, Norman F. Wiss who was a director, vice president and treasurer of this company for many years died on September 15th, 1954 leaving his widow, Mildred S. Wiss, surviving; and

"Whereas, the directors of the company feel that it is proper and fitting that recognition be made of the valuable and loyal service which he rendered to the company.

"Now, therefore, be it Resolved that the company make the following payments to the said Mildred S. Wiss:

"At the rate of $4583.33 per month (that being the salary of Norman F. Wiss at the time of his death, excluding bonuses) from September 15th, 1954 to December 31st, 1954.

"7/24ths of the bonus which would have been paid to Mr. Wiss for the year 1954 (the 7/24ths being based on the period from September 15th, 1954 to December 31st, 1954; the remaining 17/24ths of the said bonus to be paid to the executors of the estate of the said Norman F. Wiss on account of compensation for services from January 1st, 1954 to the date of his death which occurred on September 15th, 1954).

"$2750.67 per month for the two (2) year period beginning January 1st, 1955 and ending December 31st, 1956. The said payments to be made on the first day of each month beginning January 1st, 1955.

"$5,000.00; payment as a death benefit under the Internal Revenue Code."

The bonus plan referred to was instituted in 1950. After paying a bonus that year, the corporation directed its treasurer to set aside on its books the sum of $64,000 as additional compensation from which decedent was to receive $20,000 if certain conditions prevailed. The bonus plan was continued, and after an audit it was determined that the conditions required for payment of the additional amount existed for the year 1954. Decedent's estate was paid 17/24 of the $20,000 which decedent would have been entitled to had he remained with the corporation until December 31, 1954, and the petitioner received the other 7/24. The petitioner was paid the following amounts pursuant to the resolution:

	1954	1955	1956
Death benefits	$ 5,000		
7/24 of bonus		$ 5,833.33	
Periodic payments	16,000	33,008.04	$33,008.04

The payments were deducted by the corporation as business expenses. The president of the corporation who was also a member of the board testified that the payments were based in part on decedent's long and valuable service to the corporation as well as the amount of his annual income, and that the payments would not have been made had there not been an employer-employee relationship between the corporation and the decedent.

There was also some testimony that the transfer was intended as a gift, and that it was made in order to help petitioner financially during the period of transition following her husband's death. The president also testified, however, that the second resolution was adopted authorizing payment without the petitioner's needs being discussed, and no concern was shown for income that she had from other sources. The petitioner reported as income in the form of dividends, interest and gains from the sale or exchange of property $35,376.90 in the year 1955 and $37,089.67 for 1956. Petitioner was never employed by the corporation, and there was evidence in the record that decedent's salary at the time of death was a fair and reasonable one. But these and other facts which the petitioner presses need not be reviewed in detail, for what we have outlined above clearly indicates that the conclusion of the Tax Court was a permissible one.

The petitioner cites a number of decisions in support of her position. Several of them, Olsen v. Commissioner, F.2d (C.A.8, 1962); United States v. Frankel, F.2d (C.A.8, 1962); Kuntz v. Commissioner, F.2d (C.A.6, 1962); Poyner v. Commissioner, F.2d (C.A.4, 1962); and United States v. Kasynski, 284 F.2d 143 (C.A.10, 1960), were handed down after *Duberstein*. A review of these de-

cisions does little more than point out the nature of our inquiry, and their inapplicability is clear, for "the question here remains basically one of fact, for determination on a case-by-case basis." Duberstein v. Commissioner, 363 U.S. at 290. We cannot exceed the narrow function assigned to us, regardless of what others have done.

The decision of the Tax Court will be affirmed.

UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 13,759

ROY I. MARTIN AND ELIZABETH E. MARTIN, *Petitioners,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

Argued March 5, 1962

Before STALEY, HASTIE and SMITH, *Circuit Judges.*

OPINION OF THE COURT

(Filed June 28, 1962)

By STALEY, *Circuit Judge.*

This appeal involves the taxability of money paid by a corporation to the widow of one of its officers. At his death, Arthur Purdy was president of A. R. Purdy Co., Inc. ("corporation"). Pursuant to a resolution passed by its board of directors, the corporation paid decedent's widow, petitioner,[1] $32,727.24 in 1955 and $27,272.76 in 1956. Petitioner failed to report these payments as income on her tax returns, causing the Commissioner to assess a deficiency against her on the basis that they were subject to treatment as ordinary income. The Tax Court upheld the Commis-

[1] The petitioner, Elizabeth E. Martin, was married to Roy I. Martin in 1955. The husband is a petitioner on this appeal because joint income tax returns were filed for the years in question. All future references will be to the wife-petitioner only.

sioner, concluding that petitioner failed to establish that the payments constituted a gift.[2]

On this appeal, petitioner contends that the Tax Court misinterpreted the Supreme Court's decision in Commissioner v. Duberstein, 363 U.S. 278 (1960), as announcing a new rule for determining when payments by a corporation to a widow constitute a gift, and that under the holdings in pre-*Duberstein* Tax Court decisions, the payments here clearly constituted a gift. The Commissioner's position, also based on *Duberstein*, is broken down into two parts. First, the controlling question is why the transfer was made, and that if made from "detached and disinterested generosity, * * * out of affection, respect, admiration, charity or like impulse," it is a gift, while if the payment is for past services, it receives income treatment. Next, the Tax Court's resolution of that question is a factual one that must be affirmed unless clearly erroneous.

This court recently had occasion in Smith v. Commissioner, F.2d (C.A.3, 1962), to review the decision in Commissioner v. Duberstein, supra, and United States v. Kaiser, 363 U.S. 299 (1960). We said that, under those decisions, determination of whether a transfer constitutes a gift is a factual one that rests in the first instance with the trier of fact. That determination is to be made in light of all the relevant facts and circumstances and must be affirmed unless clearly erroneous.

We cannot say, from our review of the record, that the Tax Court's finding is clearly erroneous or charge it with relying on facts not relevant to the inquiry.

The corporation was closely held. Immediately

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[2] 36 T.C. No. 56 (1961).

prior to Arthur Purdy's death, its outstanding stock was held as follows:

Stockholder	Common Stock	Preferred Stock
Trust under Will of Ethel B. Purdy (deceased's mother)	588	588
Deceased	2,282½	2,282½
Elizabeth Purdy Shaw (deceased's sister)	1,825½	1,825½
Ralph W. Shaw, Jr. (deceased's brother-in-law)	304	304

Under Ethel B. Purdy's trust, upon deceased death the trust was to terminate, whereupon one-half of the corpus was to pass to deceased sister, and one-half was to be placed in trust for deceased children, the trustee being Ralph W. Shaw, Jr., deceased's brother-in-law. The deceased placed his shares of stock in the corporation into two trusts, the trustees of which were the petitioner and a corporate trustee.

Within seven days after death ensued, decedent was succeeded as president by Ralph W. Shaw, Jr., his brother-in-law, and petitioner was elected to the board. Shortly thereafter, the board unanimously passed a resolution which in pertinent part read:

> "Whereas, Arthur R. Purdy, President of this Company, died on November 3, 1954 and
>
> "Whereas, he had been associated with the Company for more than 18 years and had rendered loyal and faithful service to the Company, and
>
> "Whereas, the Directors believe that recognition of such service should be made and that his salary should be paid for a reasonable period of time to his widow * * *."

The Minutes of the meeting stated:

> "* * * In view of Mr. Purdy's long and loyal service to the Company, the officers thought that his salary should be continued to be paid to his widow * * * for a reasonable period of time after his death in recognition of such service."

The resolution went on to provide that deceased's salary should be continued for a twenty-four month period and paid to petitioner in equal monthly installments. Two board members who supported the resolution testified before the Tax Court. One testified that the payments were "based upon the past services of Mr. Purdy." The other one, an assistant vice-president of a bank, said that he was a board member in order to help protect the bank's interests, and testified that he had met the petitioner only once and that he voted for the payments because "the services that the late Mr. Purdy had rendered to the company justified the payment on its part." He also testified that when considering the resolution, he possessed little knowledge about petitioner's financial position, although he was aware that the corporation had not been paying dividends. The corporation's year-end surplus for 1955 was $801,845.52, and $828,450.82 for 1956.

The monthly payments, equal to the amount paid decedent as a monthly salary at the time of his death, were made on regular employees' payroll checks. They were deducted as business expenses by the corporation. The 1955 payments were included in the corporation's workmen's compensation policies, and subjected to withholding tax by the corporation which was reflected on a Withholding Tax Statement, commonly known as a "W-2," issued by it at the end of the year. The cor-

poration did not withhold tax for 1956 after petitioner executed a hold harmless agreement on its behalf.

The clear force of these facts is that the payments were made by the corporation as additional compensation for the deceased's services. Petitioner cites many cases to us, but a situation of this kind involving, as it does, the resolution of a purely factual question makes precedent of little value.

The decision of the Tax Court will be affirmed.

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